Commissioner Mairead McGuinness
Directorate-General for Financial Stability, Financial Services and Capital Markets Union
European Commission
1049 Bruxelles
Belgium

30 November 2020

Dear Commissioner McGuinness

Equivalence of UK derivatives regulated markets under EMIR Article 2a

FIA, ISDA, AFME, ICI, AIMA, EBF and EFAMA (together the Associations) welcome the European Commission's **(the Commission)** timely and temporary equivalence decision from 21 September 2020 with respect to UK central counterparties **(CCPs)** and subsequent recognition decisions by ESMA of CCPs and the recent temporary equivalence decision for UK Central Securities Depositories **(CSDs)** under CSDR. Together, these steps have provided much needed certainty for continued and uninterrupted access to these CCPs and CSDs by EU clearing members and EU firms.

However, **equivalence decisions are still outstanding in other critical areas of financial services, including in relation to UK regulated markets under EMIR Article 2a.** This is a standalone issue, for EU EMIR purposes only, and can be addressed independently of the wider question of recognition of UK regulated markets for other purposes.[1] The failure to grant equivalence determinations for UK regulated markets for the purpose of EMIR Article 2a before the end of the transition period will result in negative impacts for EU market participants and EU derivatives markets, create an **uneven playing field and operational challenges for EU banks and investments firms** (as explained below) and will ultimately impact corporate end-users and the real economy in the EU.

UK regulated markets offer for trading a broad range of exchange-traded derivatives **(ETDs)** that are widely used for risk-management purposes by market participants in the EU and elsewhere. In many cases, UK regulated markets provide market users with uniquely deep and liquid markets with global participation (and hence a wider number of potential counterparties) and there is no direct substitute for some UK ETDs on regulated markets in the EU or in other third countries. EU firms are major users of these markets for hedging/risk mitigation purposes as well as investing.

Derivatives traded on non-equivalent third-country regulated markets are regarded as "OTC derivatives" under EMIR.[2] In the absence of equivalence under EU EMIR Article 2a, ETDs traded on UK regulated markets will be considered as OTC derivatives after the end of the transition period for the purposes of determining (i) whether small financial counterparties **(SFCs)** have breached the clearing threshold to become financial counterparties **(FCs)** or (ii) whether non-financial counterparties **(NFCs)** have breached the clearing threshold to become NFC+s.

Adverse impacts of re-classification as an FC or NFC+ include (i) an SFC being treated as an FC would result in its transactions being subject to mandatory clearing under the EMIR clearing obligation for the first time; (ii) a counterparty being treated as an NFC+ may result in its transactions being subject to mandatory clearing under the clearing obligation, bilateral exchange of margin and other risk mitigation obligations under EMIR; (iii) the NFC+'s inability to rely on an FC to mandatorily report OTC derivatives transactions under EMIR on its behalf,[3]; and (iv) certain transactions of such FC or NFC+s may become subject to the derivatives trading obligation under EU MiFIR. The Associations' members also point to resulting market inefficiencies and fragmentation of liquidity pools and emphasize that this represents both a threat to end users' ability to manage risk, and a consequent impediment to corporate investment if NFCs decide to reduce their positions in UK ETDs to avoid becoming NFC+s.

In a letter to Executive Vice-President Dombrovskis from 28 February 2019, we described the above consequences in greater detail. The letter can be found here: https://www.fia.org/sites/default/files/2020-

---

[1] Please note that while this letter focuses on the need for equivalence under Article 2a EMIR, the Associations continue to believe that equivalence determinations should also be made in other areas. The Associations are happy to discuss these with the Commission but in the interests of brevity we have limited the scope of this letter to equivalence under EMIR Article 2a.

[2] See EMIR Article 2a and Article 2(7).

[3] Under EMIR Refit, FCs are required to report OTC transactions on behalf of NFC-s (new Article 9(1a)-(1e) of EMIR) but it is not mandatory for FCs to report on behalf of NFC+s, SFCs or FCs.

02/Brexit%20Joint%20Associations%20Letter%20on%20Equivalence%20of%20Trading%20Venues%20under%20EMIR%20and%20MiFIR.pdf

The UK Government announced, on 9 November 2020 , that it was issuing equivalence decisions for EEA exchange traded derivatives under UK EMIR Article 2a at the end of the transition period, which will enable UK firms to continue to treat derivatives traded on EEA regulated markets as ETDs rather than OTC derivatives. This will provide UK firms with benefits that include:

- Non-application of clearing and risk mitigation obligations under UK EMIR in respect of derivatives executed on EEA regulated markets (given that these trades will continue to be treated as ETDs);
- NFCs and FCs established in the UK will only have to take into account OTC derivatives and not ETDs traded on EEA regulated markets for the purposes of determining whether they exceed any relevant clearing threshold and hence will be able to continue to use their existing methodologies and inputs. The result will be that they will not change their regulatory classification solely as a result of the change of recognition of certain regulated markets;
- UK FCs that calculate their positions against the clearing thresholds in order to determine whether they are SFCs will only have to take into account OTC derivatives and not ETDs traded on EEA regulated markets and can therefore avoid the clearing threshold; and
- The UK's Financial Conduct Authority (FCA) has confirmed that firms do not need to take any action to benefit from this decision and that it will publish a list of all regulated markets under UK EMIR and equivalent third country markets before the end of the transition period.

The consequences of the UK equivalence decision and the absence of an equivalence decision by the EC include:

- An unlevel playing field for EU banks and investments firms compared to UK banks and investment firms in that those UK clients that would not be subject to the mandatory clearing and/or margining requirements when facing UK banks or investment firms, would be subject to those requirements when facing EU banks or investment firms[4];
- EU counterparties subject to EU EMIR will face a potential change in their status and hence obligations under EU EMIR, placing them in a disadvantageous position due to

[4] This is due to EU banks and investment firms being subject to EU EMIR, therefore requiring their clients to use the EU EMIR definition of OTC derivative when providing their classification to their EU bank/investment firm. A client that tends to trade on UK derivatives venues is more likely to be an FC+ (as opposed to SFC) or NFC+ if the EU EMIR OTC derivative definition is used (meaning the client faces being subject to clearing, margining and other EMIR requirements). Assuming the client is not directly subject to EU EMIR (e.g. it is a UK client or third country client), the client could avoid the increased regulatory friction by simply trading only with UK-incorporated firms. UK incorporated firms only need the client's classification to be calculated using the UK EMIR definition, and that definition (due to the UK's equivalence decision) does not penalise trading EU or UK ETDs as such
trades do not count towards the FC+/NFC+ clearing threshold under UK EMIR.

the re-characterisation of derivatives executed on UK regulated markets as OTC derivatives from the start of 2021; and

- A potentially widespread reclassification exercise under EU EMIR, which could result in mismatched classification under (a) EU EMIR and (b) UK EMIR. Not only will this cause significant confusion in the market, it will require costly and time-consuming updates to trading and other systems. This impact is exacerbated because these classifications apply at the level of all of the entities in a counterparty's corporate group.

We would note in passing that this issue is different to the considerations being raised in relation to the currently inconsistent trading obligations under EU MiFIR and UK MiFIR (**DTO**), which have been addressed in other submissions by industry bodies. This letter only concerns the recognition of UK regulated markets for purposes of the EU EMIR definition of "OTC derivatives".

Therefore, we strongly recommend to the Commission to issue equivalence determinations under EMIR Article 2a, at the earliest possible opportunity and, in any case, before the end of the transition period, in order to ensure that EU firms (whether as clients or financial services providers) can benefit from treatment similar to that available to firms established in the UK, avoiding unintended consequences that would have an impact on their risk management or investment activities.

Yours sincerely,

Walt Lukken President and CEO, FIA

Scott O'Malia, CEO International Swaps and Derivatives Association

Adam Jacobs-Dean
Managing Director, Global Head of Markets Regulation
Alternative Investment Management Association

Wim Mijs, CEO European Banking Federation

Michael Cole-Fontayn
Chairman, The Association for Financial Markets in Europe

Patrice Berge-Vincent, Managing Director, ICI Global
About the Associations

Tanguy van de Werve, Director General, EFAMA

About FIA

FIA is the leading global trade organization for the futures, options and centrally cleared derivatives markets, with offices in Brussels, London, Singapore and Washington, D.C. FIA's membership includes clearing firms, exchanges, clearinghouses, trading firms and commodities specialists from more than 48 countries as well as technology vendors, lawyers and other professionals serving the industry. FIA's mission is to:

- support open, transparent and competitive markets,
- protect and enhance the integrity of the financial system, and
- promote high standards of professional conduct.

As the leading global trade association for the futures, options and centrally cleared derivatives markets, FIA represents all sectors of the industry, including clearing firms, exchanges, clearing houses, trading firms and commodities specialists from more than 48 countries, as well as technology vendors, lawyers and other professionals serving the industry.

About ISDA
Since 1985, ISDA has worked to make the global derivatives markets safer and more efficient. Today, ISDA has more than 900 member institutions from 69 countries. These members

comprise a broad range of derivatives market participants, including corporations, investment managers, government and supranational entities, insurance companies, energy and commodities firms, and international and regional banks. In addition to market participants, members also include key components of the derivatives market infrastructure, such as exchanges, intermediaries, clearing houses and repositories, as well as law firms, accounting firms and other service providers. Information about ISDA and its activities is available on the Association's website: www.isda.org. Follow us on Twitter @ISDA.

About ICI Global

ICI Global carries out the international work of the Investment Company Institute, the leading association representing regulated funds globally. ICI's membership includes regulated funds publicly offered to investors in jurisdictions worldwide, with total assets of US$33.8 trillion. ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of regulated investment funds, their managers, and investors. ICI Global has offices in London, Hong Kong, and Washington, DC.

About AIMA

The Alternative Investment Management Association (AIMA) is the global representative of the alternative investment industry, with more than 1,900 corporate members in over 60 countries. AIMA's fund manager members collectively manage more than $2 trillion in hedge fund and private credit assets.
AIMA draws upon the expertise and diversity of its membership to provide leadership in industry initiatives such as advocacy, policy and regulatory engagement, educational programmes and sound practice guides. AIMA works to raise media and public awareness of the value of the industry.
AIMA set up the Alternative Credit Council (ACC) to help firms focused in the private credit and direct lending space. The ACC currently represents over 100 members that manage $350 billion of private credit assets globally.
AIMA is committed to developing skills and education standards and is a co-founder of the Chartered Alternative Investment Analyst designation (CAIA) – the first and only specialised educational standard for alternative investment specialists. AIMA is governed by its Council (Board of Directors).

About AFME

The Association for Financial Markets in Europe (AFME) is the voice of all Europe's wholesale financial markets, providing expertise across a broad range of regulatory and capital markets issues.

We represent the leading global and European banks and other significant capital market players.

We advocate for deep and integrated European capital markets which serve the needs of companies and investors, supporting economic growth and benefiting society.

We aim to act as a bridge between market participants and policy makers across Europe, drawing on our strong and long-standing relationships, our technical knowledge and fact-based work.

About EBF

The European Banking Federation is the voice of the European banking sector, bringing together national banking associations from 45 countries. The EBF is committed to a thriving European economy that is underpinned by a stable, secure and inclusive financial ecosystem, and to a flourishing society where financing is available to fund the dreams of citizens, businesses and innovators everywhere. Website: www.ebf.eu Twitter: @EBF

About EFAMA

The European Fund and Asset Management Association (EFAMA): EFAMA, the voice of the European investment management industry, represents 28 Member Associations, 60 Corporate Members and 23 Associate Members. At end Q2 2020, total net assets of European investment funds reached EUR 17.1 trillion. These assets were managed by almost 34,200 UCITS (Undertakings for Collective Investments in Transferable Securities) and more than 29,100 AIFs (Alternative Investment Funds).